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SUBJECT: TRANSNISTRIAN POLITICAL ECONOMY: THE CASE OF MMZ

REF: CHISINAU 48

Classified By: Ambassador Michael D. Kirby for reasons 1.4(b) and (d)

¶1. (C) SUMMARY: Despite the economic and political challenges of doing business in Transnistria (TN), Moldova Metal Works (MMZ) managed to produce a record volume of steel in 2007. The case of MMZ highlights the complicating role that economic interests play in negotiating a resolution to the TN conflict. Chisinau has honored its commitment to facilitate legal trade for registered TN companies. Moldovan export controls have caused MMZ to lose money. On the political front, the TN Supreme Soviet (parliament) will soon review "President" Smirnov's line-item veto of the 2008 TN budget. The outcome of this dispute between the TN legislature and executive may indicate who has more power (and Moscow's support) inside Transnistria. END SUMMARY.

¶2. (C) On January 18, econoff met with Andrei Yudin, MMZ General Director and a member of the Transnistrian Supreme Soviet, to discuss the company's performance, internal TN economic and political conditions, and relations with Chisinau. As in previous meetings, Yudin was frank and open. Although econoff had no problems entering TN (having informally "notified" Tiraspol of the visit), Yudin commented that the meeting had prompted inquiries to him from the TN authorities.

#### THE BUDGET BATTLE FROM THE INSIDE -----

¶3. (C) The Supreme Soviet's refusal to approve spending increases for the Executive in the 2008 budget, and the securing of Russian financial assistance by Supreme Soviet Speaker Shevchuk, have widened the political divide between the Supreme Soviet and Smirnov (reftel). Yudin, an independent member of the Supreme Soviet aligned with Shevchuk's Obnovlenie Party, said he supported cutting appropriations for the Executive, citing TN's economic hardships and, most importantly, his company's interests. He said he could not support an increase for the Executive when TN had suspended payments to state workers and pensioners, the drought had wiped out most crops, and inflation continued to mount. Asked about Smirnov's line-item veto of the 2008 budget, Yudin said the Supreme Soviet would review the budget law at the end of January. He agreed that Obnovlenie had sufficient votes (a 2/3 majority) to overcome the president's veto, but commented that Shevchuk was negotiating with Smirnov because political life must go on.

#### CALCULATING TRANSNISTRIAN TAXES: NOT AN EXACT SCIENCE -----

¶4. (C) Yudin said that MMZ paid about USD 26 million in taxes

in 2007, making the company one of the largest sources of tax income for Tiraspol. He believed that, because the company had paid a dividend in 2007, the TN authorities would increase his taxes for 2008 to USD 30 million. Yudin argued that TN's Soviet-style tax system needed to be modernized and revenues spent in a more rational manner. He opined that mounting social costs, a declining population, and declining income from privatizations, which had traditionally comprised about half of TN's yearly budget, would continue to be major concerns for TN's economy.

#### MMZ'S PRODUCTION INCREASES, CHISINAU FACILITATES TRADE

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15. (C) Yudin confirmed that 2007 was a record year for MMZ, noting that industry sources were amazed at the aging mill's ability to increase production and maintain high quality. In 2007, MMZ produced 965,198 tons of rolled and finished steel (split between reinforcing bars and steel wire rod), a 43% increase compared to 2006. MMZ exported 934,000 tons of steel products in 2007, sending 53% to CIS countries and 47% to other markets, mostly the EU. However, Yudin noted that the mill needed major capital investments for maintenance and new equipment.

16. (C) When asked about relations with Chisinau, Yudin acknowledged that the Government of Moldova (GOM) had kept its promise to facilitate trade for registered TN enterprises. He said politicians in Chisinau enjoyed lauding their own efforts, but refused to recognize the additional costs or uncertainty of the situation. Yudin complained that MMZ had paid an estimated USD 15 million in additional rail transportation costs because of Chisinau's efforts to control TN exports. Also, because of a lack of dialogue between Chisinau and Tiraspol, he'd been forced to solve political problems. For example, following Chisinau's demand to control production inputs for products bound for the EU with Moldovan certificates of origin, Yudin claimed he discreetly invited Moldovan Customs officials to his plant for an inspection. MMZ and Chisinau negotiated a reporting mechanism that combined paper and electronic notification of import documents with physical inspections of exports transported via right-bank controlled territory in order to satisfy the GOM's demands.

17. (C) COMMENT: Yudin remains willing to engage with us and comment on the challenges of doing business in Transnistria. He's an outsider who admits he's only involved in local politics at the behest of MMZ's Russian and Ukrainian investors. He asked several times about our opinion of Shevchuk, noting that he was a young leader who wanted to improve TN's economy. However, Yudin said that Shevchuk was often constrained by internal TN politics and that he (Yudin) had offered to be a surrogate in the Supreme Soviet, proposing controversial economic reforms on Shevchuk's behalf. Yudin acknowledged that Chisinau had honored its promises to facilitate trade for registered companies. However, Yudin seems to have little trust in Chisinau authorities. He noted that Chisinau could impose new demands at a moment's notice that would impede his ability to do business. We don't sense that Chisinau officials have succeeded in gaining the confidence of TN's business leaders.

END COMMENT.

KIRBY